No. 94-1995

(3)

Supreme Court, U.S.
FILED
AUG 15 1995
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

THE NEW JERSEY DIVISION OF THE RATEPAYER ADVOCATE,

Petitioner,

—v.—

FREEHOLD COGENERATION ASSOCIATES, L.P., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITIONER'S REPLY

THEODORE C. GRANGER,
DEPUTY PUBLIC ADVOCATE
DIVISION OF THE RATEPAYER
ADVOCATE
31 Clinton Street, 11th Floor
P.O. Box 46005
Newark, New Jersey 07101
(201) 648-2690

August 15, 1995

BEST AVAILABLE COPY

14pp

TABLE OF CONTENTS

PAGE

TABLE OF AUTHORITIES iii

PETITIONER'S REPLY 1

I. Respondent's Contention, that "Other High Appellate" Court Decisions Are Consistent with the Decision of the Third Circuit, Is Incorrect ... 1

II. Respondent's Contention, That Recent Decisions of FERC Interpreting PURPA and its Regulations Are Consistent with the Third Circuit's Decision, Is Incorrect 4

III. Respondent's Contention, That the Estimates of a Large Disparity Between the Relevant PURPA/FERC Avoided Cost and the Rates to Be Paid under the Power Purchase Agreement Are Unsubstantiated, Should Be Disregarded 6

IV. The Disparity Between the Relevant Board-approved PURPA/FERC Avoided Cost and the Purchase Rate of the Power Purchase Agreement Is Not Only Relevant, But It Is Fundamental to the Issues in This Case 7

V. Contrary to Respondent's Contention, the Federal Courts Even Under *Bristol Energy* Did Not Have the Jurisdiction or Statutory Basis to Halt the Board from an Attempt to Implement PURPA and FERC's Rule Against Recovery of a Purchase Price Exceeding the Relevant PURPA/FERC Ceiling from the Customers of the Utility 8

PAGE

VI. Respondent's Claim That *Duignan v. United States* Bars Raising a Jurisdictional Issue on Appeal Is Incorrect 9

CONCLUSION 10

TABLE OF AUTHORITIES

Cases PAGE

Bristol Energy Corp. v. N.H. Public Utils. Comm'n, 13 F.3d 471 (1st Cir. 1994) 8, 9

Duff v. Trenton Beverage Co., 4 N.J. 595, 607, 73 A.2d 578 (1950) 8

Duignan v. United States, 274 U.S. 195, 200 (1927) 7, 9

Indep. Energy Producers Ass'n v. Cal. Pub. Utils. Comm'n, 36 F.3d 848 (9th Cir.1984) 1, 3

Smith Cogeneration Management, Inc. v. Corp. Comm., 863 P.2d 1227 (Okla.1993) 1, 2, 3

Administrative Cases

Conn. Light and Power Co., 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,034 (1995) 4, 5, 6

New York State Elect. & Gas Corp., 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,027 (1995) 4

West Penn Power Co., 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,153 (1995) 4, 5

Statutes

Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 (1992), 16 U.S.C. § 2621(d)(10) 8, 9

The Public Utility Regulatory Policies Act of 1978 ("PURPA") § 210, Pub. L. No. 95-517, 92 Stat. 3117 (1978) ..... *passim*

PURPA Section 210(e), 16 U.S.C. § 824a-3(e) 1, 2, 5, 8, 9, 11

PAGE

Regulations

18 C.F.R. § 292.304(d) 1, 2

This reply addresses the new issues raised in Respondent's Opposition Brief.

I. Respondent's Contention, that "Other High Appellate" Court Decisions Are Consistent with the Decision of the Third Circuit, Is Incorrect. (Opposition of Freehold Cogeneration Associates, L.P. ("Opp.") at 15).

Respondent Freehold Cogeneration Associates, L.P. ("Freehold") offered two decisions to support its contention: (1) *Indep. Energy Producers Ass'n v. Cal. Pub. Utils. Comm'n*, 36 F.3d 848 (9th Cir. 1984) ("IEPA") and (2) *Smith Cogeneration Management, Inc. v. Corp. Comm.*, 863 P.2d 1227 (Okla. 1993) ("Smith"). Neither of these decisions hold that Section 210(e) of the Public Utility Regulatory Policies Act of 1978 ("PURPA") forbids state regulators from implementing the PURPA/FERC prohibition against purchase prices exceeding the relevant PURPA/FERC purchase price ceiling. Rather, they stand for these principles: **(1) Any purported action by a state regulatory commission to require a purchase price at a level other than the relevant PURPA/FERC purchase price is preempted under the Supremacy Clause of the United States Constitution and (2) a contractual long-run fixed purchase price is not entitled to protection for the term of the contract *unless* the original contract price is at the relevant PURPA/FERC price in conformity with FERC rule 18 C.F.R. § 292.304(d)(2).**

A. The *IEPA* Case. The California Public Utility Commission ("CPUC') instituted a program that authorized utilities to apply operating and efficiency standards to qualifying facilities ("QFs") and, on determining that a QF did not comply, to substitute an "alternative" avoided cost rate for the avoided cost rate specified in a standard offer contract. The "alternative" avoided cost rate was calculated at 80% of the short-term "economy" published avoided cost rate. (36 F.3d at 858). The appellant had challenged the regulations on the ground that the program was preempted by PURPA and the Federal

Energy Regulatory Commission ("FERC") regulations. (at 853). The court upheld the challenge after a traditional Supremacy Clause analysis based upon the inconsistency of the state's program with PURPA. (The decision did not rest upon PURPA § 210(e), the basis of Freehold's action, which forbids "utility-type" regulation). (at 858).

Freehold omitted the following sentence from the otherwise complete paragraph that it quoted in its Opposition (at 15 and 16): "Federal regulations provide that QFs are entitled to deliver energy to utilities at an avoided cost rate calculated at the time the contract is signed." (Cit. Omitted). The paragraph of the decision preceding the paragraph quoted by Respondent is important to the meaning of the quoted paragraph. It says that the requirement to pay *full* avoided costs in 18 C.F.R. §292.304(d) *properly balanced* Congress' desire to promote cogeneration while not burdening ratepayers by requiring them to subsidize QFs. (at 858). The complete quoted paragraph in proper context of the original decision says that the Supremacy Clause of the United States Constitution prohibits a state regulatory commission from requiring a purchase price different from the relevant PURPA/FERC avoided cost of the utility. In particular, an excessive price would vitiate this balance and transgress Congress' concern about ratepayers' subsidizing QFs.

B. The *Smith Case*. Smith Cogeneration Management proposed to build a cogeneration plant and sought (1) to have the state regulatory commission fix the estimated avoided cost before the execution of a contract which obligated the QF to deliver power and (2) to waive the commission rule which mandated a contract provision allowing the commission to change the agreement during its term. (863 P.2d at 1230, 1237). The court applied, as in the *IEPA* case, traditional preemption doctrine (at 1239), not PURPA Section 210(e), and held (1) that the state's requirement to include the contract provision allowing the state to change rates was preempted because the provision was in conflict with PURPA and the

FERC regulations which grant QFs the right to have a long-term purchase contract at a price based on the avoided cost of the utility at the time the obligation to deliver is incurred (at 1240), (2) that Smith attempted to have avoided cost established for a 15-year contract before becoming legally obligated and (3) that, therefore, Smith was not entitled to have avoided cost fixed as a contractual purchase price for the life of the proposed agreement until Smith presented a contract legally obligating itself to deliver power at the avoided cost of the utility at the time the obligation was incurred. (at 1241).

Thus, the *IEPA* and *Smith* cases say that a state is preempted from approving a purchase price inconsistent with the PURPA/FERC ceiling and a contractual purchase price is not protected over the term of the contract from realignment in accordance with the PURPA/FERC rules unless that price was set originally at the proper PURPA/FERC prescribed level. Under these principles, Freehold is not entitled to have the price in the agreement protected because the price is higher than the relevant PURPA/FERC avoided cost of the utility at the time the agreement was presented for approval. The creation of a legal obligation was conditioned (1), by the regulations of the New Jersey Board of Public Utilities ("Board"), on the review and approval of the contract by the Board and (2), by the explicit agreement of the parties, on approval by the Board of all the terms exactly as stated in the agreement. *These conditions were impossible* to fulfill since the specified price exceeded the relevant PURPA/FERC ceiling and the Board was preempted from implementing that higher price in violation of the ceiling. The utility's avoided cost had dropped substantially from 1989 (when negotiations began) to 1992 (when the contract was signed). The Freehold contract had not incorporated the proper Board-approved avoided cost of the utility in 1992 in accordance with the *Smith* case. Hence, the purchase price is not sheltered from further Board action implementing the PURPA/FERC price ceiling.

II. Respondent's Contention, That Recent Decisions of FERC Interpreting PURPA and its Regulations Are Consistent with the Third Circuit's Decision, Is Incorrect. (Opp. at 17)

An analysis of the reported decisions of FERC since the Third Circuit's decision, which Freehold cites, shows a severe conflict between FERC and the Third Circuit. The three decisions are (1) *New York State Elect. & Gas Corp.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,027 (1995) ("NYSEG"), (2) *West Penn Power Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,153 (1995) ("West Penn") and (3) *Conn. Light and Power Co.*, 71 Fed. Energy Reg. Comm'n Rep. (CCH) ¶61,034 (1995) ("CL&P"). These decisions concern the extent of state jurisdiction over implementation of PURPA/FERC's purchase rules and the invalidity of an agreement at a purchase price exceeding the PURPA/FERC ceiling. Specifically, with respect to the present case, they show that (1) the Board's approval of a price exceeding the relevant PURPA/FERC ceiling was null and that the agreement was void *ab initio* (the *CL&P* decision) and that (2) the Board had lawful jurisdiction over the agreement for the purpose of implementing that ceiling on behalf of ratepayers. (The *NYSEG* and *West Penn* decisions).

A. The *NYSEG* and *West Penn* decisions. Because of the similarity between the two cases, the discussion will focus on the more recent *West Penn* case. Previous to the FERC petition, lengthy litigation before the **state** regulatory commission and the **state** courts had determined that a valid, legally binding contract existed. (at 61,153). The gravamen of the petition was that the established rates in the long-term QF contracts should be recalculated if subsequent avoided cost calculations differ from the relevant PUPRPA/FERC avoided cost properly used to determine the original rates. As in the *NYSEG* case, FERC rejected the petition and refused to disturb the contract. (at 61,153). The FERC stated that it did not intend to adjudicate specific provisions of individual QF contracts and that

it was up to the states, not FERC, to determine the specific parameters of individual QF power purchase agreements, including the date at which a legally enforceable obligation was incurred under state law. The FERC also stated that whether the particular facts applicable to an individual QF necessitated modification of other terms and conditions of the QF's contract with the purchasing utility was a matter for the states to determine. (at 61,495). The FERC further noted that for specific QFs the choice of the critical date on which a legally enforceable obligation to deliver electricity is incurred is the responsibility of the states and not FERC and the fact that the determination was made after the date itself was immaterial. *Id.* FERC has declared that state implementation of the PURPA/FERC rules on the purchases and sales between utilities and QFs, such as adjudication of specific terms of the contracts and whether the specific facts require modification of terms and conditions, are matters for the states. Thus, the FERC, just after the Third Circuit decision and now, is clearly in conflict with the Third Circuit which applied PURPA Section 210(e) to abort state proceedings on these very matters. In conjunction with FERC's *West Penn* "hands-off" policy in favor of state determination of these matters, the Third Circuit decision, unless reversed, will work an injustice on the customers of the utility. The Third Circuit should have allowed the Board to proceed in the implementation of the PURPA/FERC price ceiling. The result of all this is that the New Jersey Division of the Ratepayer Advocate ("Ratepayer Advocate") will have been denied a forum and means for the implementation of the PURPA/FERC ceiling.

B. The *CL&P* decision. This important decision, issued just two days after the Third Circuit decision, supports these conclusions: **(1) PURPA mandates that a contract containing a purchase price in excess of the relevant avoided cost of the utility is void *ab initio* and (2) the treatment of such a "contract" as void *ab initio* is not inconsistent, as suggested by the Third Circuit, with the congressional pur-**

pose of PURPA to encourage the development of cogeneration. The FERC determined correctly, in the opinion of the Ratepayer Advocate, that the attempted implementation of a state statute, requiring a purchase price exceeding the PURPA/FERC ceiling, resulted in a "contract" which was void *ab initio*. (at 61,030). A ground for the decision was that the imposition of such a price is in conflict with the PURPA/FERC purchase price at the full avoided cost of the utility, the *maximum* allowed by Congress. (at 61,029). Therefore, the action of a state regulatory commission requiring that the purchase price exceed the relevant current PURPA/FERC avoided cost is null and the contract void *ab initio*. This FERC holding clearly contradicts the Third Circuit which held that, regardless of whether a state regulatory commission approved a purchase price at a level *per se* illegal and contrary to PURPA, that price is protected for the full term of the agreement. Consistency with PURPA and the *CL&P* decision would have required the Third Circuit to find the agreement void *ab initio*.

III. Respondent's Contention, That the Estimates of a Large Disparity Between the Relevant PURPA/FERC Avoided Cost and the Rates to Be Paid under the Power Purchase Agreement Are Unsubstantiated, Should Be Disregarded. (Opp. at 25).

Much documentation of the disparity between the relevant Board-approved PURPA/FERC avoided cost of the utility and the purchase price in the Freehold power purchase agreement is both in evidence before the Board proceeding *sub judice* and in the record before the Third Circuit. Freehold did not, until now, raise the issue that the documents were unsubstantiated. It is especially noteworthy that, when the Ratepayer Advocate petitioned the Third Circuit to include the very important document, FCA-18, in the record, Freehold did not oppose the motion and did not make the slightest suggestion that the document was in the least unsubstantiated.

Most recently, Freehold remained silent when the Ratepayer Advocate relied on the document in its petition for reconsideration before the Third Circuit. Freehold remained completely silent until now. By an application of the authority adduced by Freehold itself, *viz., Duignan v. United States,* 274 U.S. 195, 200 (1927), Freehold should be deemed to have waived the issue.

IV. The Disparity Between the Relevant Board-approved PURPA/FERC Avoided Cost and the Purchase Rate of the Power Purchase Agreement Is Not Only Relevant, But It Is Fundamental to the Issues in This Case. (Opp. at 19).

The disparity is relevant and fundamental to the support of the Ratepayer Advocate's case—contrary to Freehold's contention. According to the Ratepayer Advocate's **first** legal theory, since PURPA was enacted under the Interstate Commerce Clause of the U.S. Constitution, it therefore applies immediately and directly to the power purchase agreement, thus rendering null the action of the parties or any government agencies not in harmony with PURPA. The Congressional and FERC prohibition against a purchase price exceeding the utility's approved avoided cost makes any agreement in contravention of that prohibition void by virtue of the Interstate Commerce Clause. According to the **second** theory, under the law of administrative agencies, any action of a creature of PURPA (including the Board) contravening the PURPA/FERC ceiling is void as *ultra vires*. According to the **third** theory, the Board's action in approving a purchase price greater than the relevant Board-approved avoided cost of the utility violated PURPA and was preempted under the Supremacy Clause of the United States Constitution. According to the **fourth theory**, the Board had incorporated the PURPA/FERC ceiling in its own regulations, and PURPA, under §210(e)(3)(A), in the same section of PURPA upon which Freehold bases its Opposition, prohibits the Board from "exempting" QFs from its own regulations implementing the

FERC rules. Thus, PURPA preempted the Board from requiring or approving a price exceeding the PURPA/FERC price ceiling. According to the **fifth** theory, the parties agreed to have the law of New Jersey govern the agreement and that law holds directly that any contract conditioned on a price which must be approved by a regulatory agency not so empowered, as in this case, is void *ab initio. Duff v. Trenton Beverage Co.*, 4 N.J. 595, 607, 73 A.2d 578 (1950). Under any of these approaches Freehold obtained no right to have a purchase price, unlawful and in violation of public policy, perpetuated into the future.

V. Contrary to Respondent's Contention, the Federal Courts Even Under *Bristol Energy* Did Not Have the Jurisdiction or Statutory Basis to Halt the Board from an Attempt to Implement PURPA and FERC's Rule Against Recovery of a Purchase Price Exceeding the Relevant PURPA/FERC Ceiling from the Customers of the Utility. (Opp. at 23).

Freehold contends (Opp. at 24) that the jurisdictional issue in the present case is virtually identical to that in *Bristol Energy Corp. v. N.H. Public Utils. Comm'n*, 13 F.3d 471 (1st Cir. 1994) ("Bristol Energy"). In that case, the state regulatory commission sent data requests to several QFs seeking detailed disclosures of financial and proprietary information to perform a study of wholesale power supplies required by the Energy Policy Act of 1992 ("EPAct"). (at 473). The QFs alleged that the business and financial disclosure order of the state regulatory commission violated Section 210(e) of PURPA and the FERC regulation thereunder exempting QFs from state regulation of the finances and organization of electric utilities. The court followed a two-step approach. It first recognized that PURPA placed a limitation on federal jurisdiction in proceedings involving FERC's rules dealing with the purchase and sales between electric utilities and QFs. The court held, however, that those rules were not at issue in the

case because the data requests were issued pursuant to both state law and the EPAct. (465 at footnote 5). Then the court proceeded to consider whether the PUC's limited inquiry for a study mandated by the EPAct constituted state "regulation respecting . . . [t]he financial and organizational regulation of electric utilities". (at 475). The court held that PURPA Section 210(e) did not exempt the carrying into effect by a state regulatory agency of *another* Congressional mandate not involving implementation of PURPA or FERC's rules thereunder. (at 475). The court held that an inquiry mandated by Congress did not constitute "utility type" regulation. *Id.*

Application of the *Bristol Energy* two-step approach here confirms the Ratepayer Advocate's contention. To implement (1) the prohibition against exceeding the PURPA/FERC ceiling and (2) the PURPA/FERC requirement to insure that the purchase price satisfies that prohibition, the Board should be free to limit recovery to the relevant PURPA/FERC ceiling. Furthermore, even if this were deemed not to be implementation, the statutory mandate that the rules shall insure that the purchase price does not exceed the relevant PURPA/FERC ceiling may be considered comparable to the mandate of the EPAct which *Bristol Energy* held not subject to PURPA 210(e). Thus, under either of these two scenarios a QF should not be sheltered from state regulatory action limiting recovery to the relevant PURPA/FERC avoided cost of the utility. In short, Freehold has cited not a single authority which applied PURPA Section 210(e) to foreclose a state regulatory agency from implementing the PURPA/FERC prohibition against a purchase exceeding the relevant PURPA/FERC purchase price ceiling.

VI. Respondent's Claim That *Duignan v. United States* Bars Raising a Jurisdictional Issue on Appeal Is Incorrect. (Opp. at 28).

Freehold quotes from *Duignan v. United States,* 274 U.S. 195, 200 (1927) that "[i]t is only in *exceptional cases* coming

here from the federal courts that questions not pressed or passed upon below are reviewed." (Emphasis added). At the end of this quotation the string of authorities which the court cites makes clear that raising a jurisdictional argument always qualifies as one of "the exceptional cases" mentioned in the quotation and that such an argument may always be raised at any level of appeal.

CONCLUSION

For the foregoing reasons and the reasons set forth in the petition, the Court should grant a writ of certiorari on the two questions presented in the petition.

Respectfully submitted,

Theodore C. Granger
Deputy Public Advocate
DIVISION OF THE
RATEPAYER ADVOCATE
31 Clinton Street, 11th Floor
P.O. Box 46005
Newark, New Jersey 07101
(201) 648-2690

August 15, 1995